IN THE

Supreme Court of the United States

OCTOBER TERM, 1948.

No. 356.

THE CENTURY INDEMNITY COMPANY,

Petitioner,

—against—

RICHARD L. ROSENBAUM, Trustee in Bankruptcy for Ultimite Corporation, Bankrupt, and GRAYS FERRY BRICK COMPANY,

Respondents.

REPLY BRIEF FOR PETITIONER ON PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SECOND CIRCUIT.

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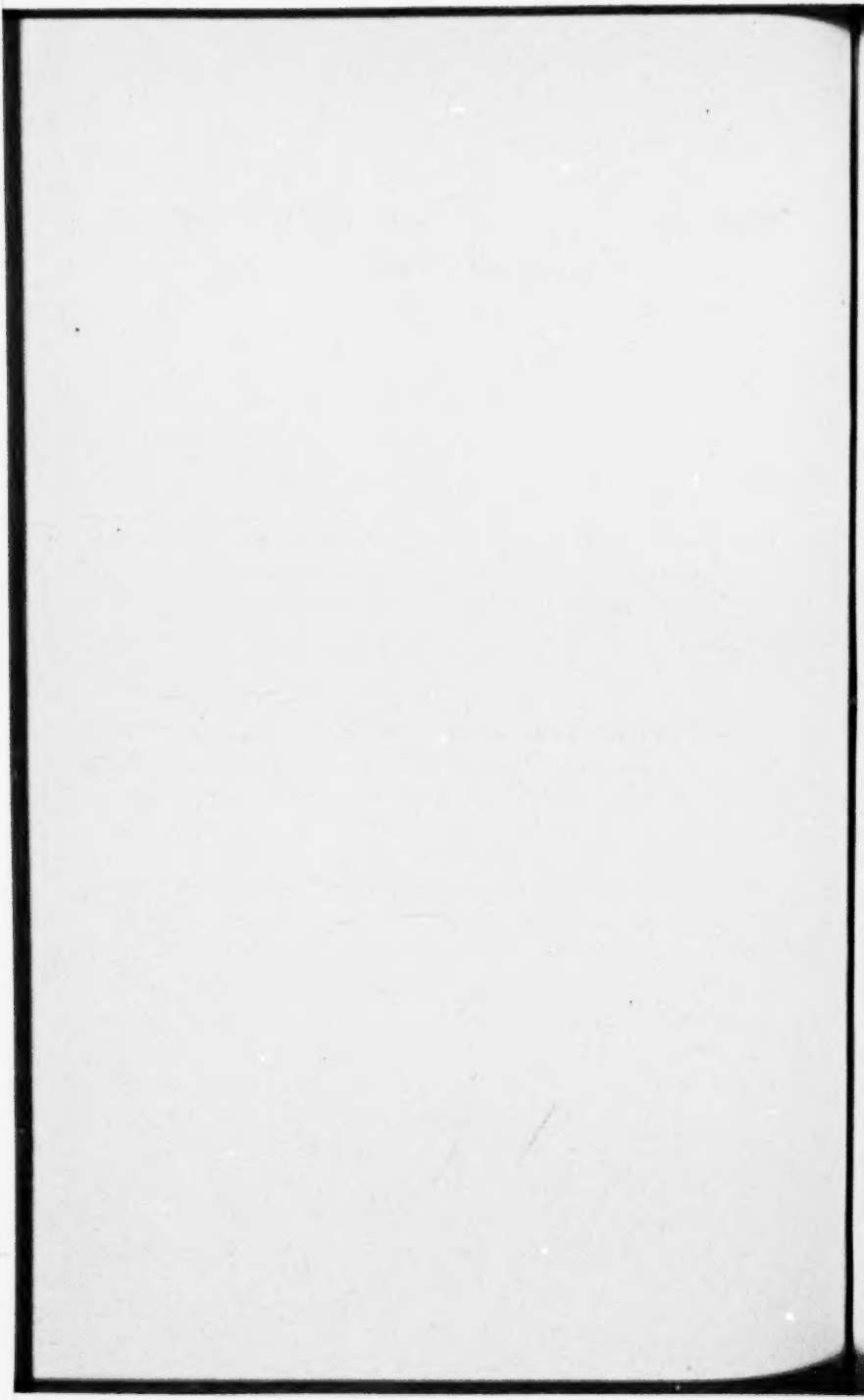

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The brief of the trustee completely begs the main issue involved in this case, namely, whether the rights of a surety on a bond given pursuant to a federal statute are to be governed by federal law or by state law. It points to no case where state law was applied to a Miller Act bond. It overlooks completely the fact that labor and material creditors on a government job and the surety, as subrogee of those creditors, have by the overwhelming weight of authority, been awarded special rights in and to the moneys arising out of a government contract because of the fact that such labor and material creditors cannot file liens against government property to protect their interests.

In the instant case neither the trustee in bankruptcy nor the judgment creditor is in the position of a bona fide purchaser for value without notice and the fund in question was created and in existence, capable of identification, before any lien was acquired by either of them (Referee's opinion, R., p. 66). The only result of the Circuit Court's decision is to make available to general creditors of the bankrupt a fund representing the final payment on a government contract when those creditors had nothing to do with the creation of that fund, to the detriment of labor and material creditors (and the subrogated surety) who because the contract was for the construction of a government building, were barred by law from filing a lien for the protection of their rights. It is this factor which underlies the entire body of federal case law on the rights of labor and material creditors and the subrogated surety on the payment bond.

In Point II of his brief, the trustee attempts to make the point that the decision of the Court below is not in conflict with the decisions of the Supreme Court or of other Circuit Courts or of the New York Courts. Yet, every case cited in petitioner's main brief under Point II and III, negatives this attempt.

The trustee, on page 11 of his brief, states that those cases cited by petitioner where the contracts were completed but in which unpaid laborers and materialmen were held to have an equitable lien superior to the claims of general creditors or assignees, to which lien the surety was subrogated upon payment, were only those in which the moneys were still in the possession of the government. This is not so.

In the following cases, all cited in petitioner's main brief, the moneys were no longer in the hands of the government, but, as here, were in the hands of the contractor's trustee in bankruptcy, and the surety was held entitled thereto ahead of the claims of the trustee, general creditors or assignees:

Cox v. *New England Equitable Insurance Company,* 247 Fed. 955;

Moran v. *Guardian Casualty Co.,* 76 Fed. (2d) 438. (The moneys here were in the hands of a receiver.);

Philadelphia National Bank v. *McKinlay,* 72 Fed. (2d) 89, cert. den. 293 U. S. 583;

In re: *L. H. Duncan & Sons,* 127 Fed. (2d) 640;

Matter of Zaepfel & Russell Inc., 49 Fed. Supp. 709, affirmed sub. nom. *Farmers State Bank* v. *Jones,* 135 Fed. (2d) 215;

London & Lancashire Indemnity Company of America v. *Endres,* 290 Fed. 98.

In the last cited case, the fund to which the Eighth Circuit held the surety entitled ahead of the trustee and all other creditors did not even involve the final payment under the contract as does the instant case. It involved, instead, extra compensation beyond the contract price voted to the bankrupt contractor by an Act of Congress.

The trustee's statement that the Miller Act and its predecessor statute does not create a lien in favor of unpaid laborers and materialmen is contrary to the overwhelming weight of authority, as evidenced by

the following decisions of the Supreme Court and other Circuit Courts cited in petitioner's main brief:

Henningsen v. *United States Fidelity & Guaranty Co.*, 208 U. S. 404;

Belknap Hardware & Mfg. Co. v. *Ohio River Contract Co.*, 271 Fed. 144;

U. S. Fidelity & Guaranty Company v. *Sweeney*, 80 Fed. (2d) 235;

Farmers Bank v. *Hayes*, 58 Fed. (2d) 34, cert. den. 287 U. S. 602;

Cox v. *New England Equitable Insurance Company*, 247 Fed. 955;

which hold that where the contractor has himself completed the contract but failed to pay for labor and material, that the laborers and materialmen, in spite of, or in addition to the giving of the bond, had an original and continuing equitable priority in the fund; that the surety was subrogated to that right and that when the surety made payment, its rights related back to the date of its bond.

Clearly the decision of the Court below in the instant case is in direct conflict with those above referred to and others not cited.

The trustee's brief also completely begs the proposition that the bankrupt had no right to the fund except to the extent that a surplus might remain after payment of labor and material creditors and to the subrogated surety, and that therefore neither the trustee nor the judgment creditor could acquire a lien on that which was not the property of the bankrupt. (*Philadelphia National Bank* v. *McKinlay* and *In re*: *L. H. Duncan & Sons*, both *supra*.)

The trustee's brief also begs the proposition that even if New York law is applicable to the rights of a federal surety (which petitioner disputes), that the New York cases cited in petitioner's main brief have consistently followed the federal rule in connection with payment bonds on New York state contracts, and that other Circuit Courts have likewise applied the federal rule to contracts of other states.

The statement by the trustee in Point III of his brief that the decisions relied upon by petitioner did not pass upon the question presented in the instant case is clearly negatived by all of the decisions cited in petitioner's main brief and particularly by those where the moneys were already in the hands of the contractor's trustee in bankruptcy and the surety was permitted to recover them.

Equally unfounded is the statement of the trustee that the decision of the Circuit Court below is of limited application and is not of general importance. The cases cited in petitioner's main brief and the many others on the same subject which were not cited, make it clear that the instant decision which is in conflict with all of those cases, disrupts completely the entire field of case law on this subject and leaves in a state of chaos and confusion the rights of labor and material creditors and their subrogated sureties on all government contracts now in existence and which may hereafter be let.

Nor is there any basis for the contention of the trustee that "the question presented has been rarely raised although the Miller Act and its predecessor Acts have been in existence over a great number of years". The many decisions on this subject negative that statement. What is important, however, is that

it has never before been resolved in the manner adopted by the Circuit Court in the instant case and for that very reason should be reviewed by this Court.

CONCLUSION.

The petition for a writ of certiorari should be granted.

Respectfully submitted,

SAMUEL GOTTESMAN,
Attorney for Petitioner.

New York City, November, 1948.